

COLLEGE OF EUROPE
BRUGES
ECONOMICS DEPARTMENT

FINANCIAL SYSTEMS AND INCOME INEQUALITY

Supervisor: Prof. Christian De Boissieu

Thesis presented by
Joana Elisa Maldonado
for the
Degree of Master of Arts
in European Economic Studies

Academic Year 2015–2016

Abstract

This thesis examines the impact of financial system structures on income inequality. In the debate on ‘real’ effects of financial systems, economic growth has been analysed in detail, while potential welfare effects on income inequality have been neglected. Against the background of a trend towards more market-based and less bank-based financial systems, this thesis presents a panel analysis of financial systems and income inequality in the European Union.

To the best knowledge of the author, there exists no comprehensive theory of financial systems and their impact, and most existing studies linking finance to income inequality consider financial development rather than the type of financial system. By adapting a model from an OECD paper by Denk and Cournède (2015) in terms of variable specifications and applying it to a sample of 27 European Union member states from 1995 to 2012, this thesis shifts the focus more specifically on differences between market-based and bank-based financial systems.

This thesis is presented in three parts — theory, model and empirical results. The first chapter lays out the theoretical grounds for analysis with a classification of hypotheses and a literature review of existing empirical studies. In the second chapter, a model is established and the data set introduced. The final chapter discusses the estimation results and interprets them in context of the academic literature and the current policy discussions concerning a Capital Markets Union in Europe.

It is found that an increase in the market-based component of a financial system leads to slightly higher income inequality as measured by the Gini coefficient. However, the effect is small and not robust to alternative measurement by the S80/S20 ratio. Decomposing income growth by quintiles does not detect an influence of changes in the market-based component. Increases in the bank-based component negatively affect income growth across the income distribution.